

X. KEY OBSERVATIONS AND LESSONS LEARNED

Key Observations

1. There are multiple reasons why community benefit reporting varied across the demographics. The study observed differences in a demographic group's general treatment of an activity as community benefit (e.g., lower percentages of high population hospitals generally treated Medicare and other shortfalls as uncompensated care than did other hospitals) and varying costing methodologies used by the hospitals. Undoubtedly other factors, including many not analyzed in this study, contributed to these variations. These factors and limitations must be considered when reviewing the study's findings. The new Form 990 Schedule H reporting should reduce much of this variation in reporting.
2. Any revised standard would affect the different types and sizes of hospitals differently depending upon the types of activities required to be taken into account as community benefit, the quantitative measure (if any), and the extent to which it provides exceptions or special rules to address special circumstances and demographics (e.g., an exception from a quantitative standard if the nonprofit hospital is the sole provider in the community).
3. A significant percentage of the hospitals in the study reported uncompensated care and aggregate community benefit expenditures that were below various "percentage of revenues" levels. For example, although the reported data is subject to a number of limitations, the data indicates that a significant percentage of all types and sizes of hospitals in the study would fail to satisfy an exemption standard requiring uncompensated care expenditures of at least 3% of total revenues, or aggregate community benefit expenditures of at least 5% of total revenues. In large part, this is attributable to the concentration of uncompensated care and aggregate community benefit expenditures in a relatively small number of hospitals. The data also suggests that an attempt to draw bright lines could have disproportionate impacts on hospitals depending upon their size, where they are located, their community benefit mix, and other hospital and community demographics.
4. Financial capacity also varied within the sample. In general, smaller hospitals, including CAHs, had lower profit margins than larger hospitals in the study. Also, the percentage of hospitals reporting deficits decreased as revenue size increased.
5. Those respondent hospitals that reported information regarding how they established executive compensation, including use of the rebuttable presumption procedure, almost unanimously reported that they complied with key elements of that procedure. High levels of compliance with the procedure were confirmed in the examinations. The hospitals selected for examinations generally were selected because they reported executive compensation amounts at relatively high levels compared to other hospitals of similar size and type. The traditional

risk analysis and examination methodologies used in these examinations confirmed widespread compliance with reasonable compensation standards. More work must be done to assess the impact that the rebuttable presumption procedure (including the use of for profit comparables) and the initial contract exception (which provides that the Section 4958 excise tax does not apply to an initial contract between an organization and a disqualified person) are having on establishing executive compensation amounts and the ability of the IRS to challenge compensation paid by many tax-exempt organizations.

6. Beginning with the 2009 tax year (2010 filing season), the Form 990, Schedule H, *Hospitals*, should promote uniform and accurate reporting of quantitative and qualitative community benefit information by tax-exempt hospitals. Looking ahead, particular areas of inquiry are expected to include the following: (a) accuracy of costing methodologies used to measure community benefit; (b) medical research funded by for-profit organizations or not made widely available to the public; (c) amounts reported as bad debt that are actually attributable to charity care; (d) treating portions of Medicare shortfalls or certain community building activities as community benefit; and (e) review of non-quantifiable aspects of community benefit.

Lessons Learned

1. Many of the questionnaire's questions proved to be ambiguous or difficult to answer without a supplemental explanation, and some were criticized as being judgmental or value laden. In future initiatives, the IRS will strive to work more closely with other experts in designing the questions to be asked of the respondents in the study, and will consider using pilots and samples to test a draft questionnaire before implementation of the final questionnaire.

2. Studies of this nature are subject to disclosure rules designed to prevent direct or indirect disclosure of a taxpayer's identity or taxpayer information. This caused the IRS to combine or omit certain data in the report, or sometimes use general descriptions by using terms such as "nearly all" or "a few" instead of referring to specific numbers or percentages. This was especially true in the case of the study's reporting of executive compensation examinations. The IRS will more carefully consider disclosure issues at the front end as it designs future questionnaires and studies.

3. The comprehensive nature of the study and the large volume of data received, including significant amounts through narrative descriptions and attachments, resulted in it taking longer to analyze the data and complete the report than was expected. The release of an interim report to summarize the aggregate data as reported to the IRS proved to be a valuable tool, both in helping the IRS determine which areas required further work, and in assuring transparency to the public regarding the process. The IRS anticipates using interim reports in those future compliance initiatives it expects will take a substantial period of time to complete. Further, studies of this nature require

dedication of significant resources of IRS personnel that must be trained for the study's specific tasks, and more training specific to the study should be built in at the front end of these initiatives to maximize the quality and quantity of information obtained from the study.

4. The questionnaire's response rate was high and the overall quality of responses was very good. The quality of the report is of course dependent on the quality of responses and the willingness of the respondents to participate in the study. The IRS will study ways to assure that response rates remain high in future initiatives.

5. In areas where the tax-exempt organizations being studied operate in competition with or along side of for-profit organizations, it would also be helpful to have a deeper understanding of those for-profit organizations. Future initiatives should attempt to take into account relevant studies or other bodies of knowledge regarding such organizations, whenever possible.

6. The classification of respondents into various categories to analyze reported data across certain demographics is helpful and interesting, but its utility depends upon the soundness of the classifications. Although some classifications cannot be determined until the data is received and preliminarily analyzed, to the extent possible, the IRS should build possible classification criteria into the design of the initial questionnaire.